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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20054

APR 12 1996

In the Matter of)

Federal-State Joint Board on)
Universal Service)

CC Docket No. 96-45

COMMENTS OF
WINSTAR COMMUNICATIONS, INC.

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WINSTAR COMMUNICATIONS, INC.**

WinStar Communications, Inc. ("WinStar"), by its undersigned counsel and pursuant to Section 1.415 of the Commission's rules, submits these comments in response to the Commission's Notice of Proposed Rulemaking and Order Establishing a Joint Board in the above captioned proceeding.

INTRODUCTION

WinStar is a publicly traded company on the NASDAQ. It develops, markets and delivers telecommunications services in the United States. Over the last five years, WinStar has grown rapidly.¹ The Company's local telecommunications services are offered in 43 of the nation's largest metropolitan statistical areas. The company provides local telecommunications services on a point-to-point basis using 400 megahertz ("MHz") of wireless, digital millimeter wave capacity in the 38 gigahertz "(GHz)" band, a configuration referred to as Wireless FiberSM. WinStar has been approved for competitive local exchange carrier service operations in California, Florida, Illinois, Massachusetts, New York , Washington, and Tennessee and has

¹ WinStar had over 300 full-time employees in 1995 and expects to add an additional 200 in 1996.

applications pending in six other states including Arizona, Connecticut, Georgia, Maryland, Michigan and Texas. WinStar has also received authority to operate as a competitive access provider in 21 states² and has applications pending in a number of states.³ Using this wireless backbone gives WinStar far greater flexibility and responsiveness than the traditional wireline networks of incumbent local exchange carriers. The passage of the Telecommunications Act of 1996 should hasten WinStar's ability to provide such competitive services.

In addition, WinStar owns several other communications-related entities that provide switchless and switched long distance services on a resale basis throughout the United States as well as other enhanced services including 800 service and prepaid phone cards. Another WinStar affiliate, WinStar New Media Company, Inc., provides information services and produces non-fiction video products primarily for the educational and historic content markets.

As a new entrant into the local telecommunications market, and an entrant using Wireless FiberSM rather than traditional wireline facilities, WinStar has an immediate interest in the Commission and Joint-Board's inquiry into universal service support mechanisms. WinStar believes that competition promotes universal service because it provides significant economic incentives to reduce prices and lower service costs. Universal service support mechanisms, however, can have a profound impact on local telephone competition. Obviously, if universal service support is made available only to incumbent local telephone companies, new entrants will be unable to compete in the market. Similarly, if universal service support obligations are imposed disproportionately on new entrants, competition will not emerge. WinStar urges the Commission and the Joint-Board to develop universal service support principles and

² California, Colorado, Connecticut, Florida, Georgia, Illinois, Kansas, Maryland, Massachusetts, Minnesota, Missouri, Nebraska, New York, Ohio, Pennsylvania, Texas, Washington, Wisconsin, Michigan, Indiana, and Tennessee.

³ States with pending applications include Arizona, Louisiana, New Jersey, New Mexico, North Carolina, Oklahoma, Oregon, Utah, and Virginia.

mechanisms that minimize any adverse competitive impacts and apportion responsibility for universal service support on a competitively neutral basis.

I. HOW MUCH SUPPORT IS NECESSARY IN A COMPETITIVE ENVIRONMENT?

With the exception of specific directions for schools, libraries and rural health care providers, the Telecommunications Act of 1996⁴ does not mandate a specific universal service support mechanism, but gives the Commission and the Joint-Board broad latitude in developing such a mechanism. At a fundamental level, the Commission and Joint-Board should begin by asking how much universal service support is necessary in a competitive market.

Competition enhances universal service because it provides incentives for firms to reduce both prices and costs. Certainly, WinStar expects to enter the local telecommunications market with competitive prices and costs. WinStar believes that its services will be attractive to a large number of customers and, thus, will encourage individuals to subscribe to telephone service. Likewise, WinStar's presence in the market should encourage incumbent providers to offer services at competitive rates and to enhance their efficiencies. Said differently, in an effectively competitive market, an incumbent is unlikely to respond to WinStar or any other competitor by raising its prices to unaffordable levels, degrading its service quality or inflating its costs. Competition plainly promotes universal service.

Clearly, it is inappropriate to develop universal service subsidies that are intended to maintain incumbent prices and costs above the market level or otherwise maintain incumbent revenues or profits. For example, if the incumbent telephone provider charges \$24 a month for local telephone service, and a competitor enters the market and provides service for \$22 a

⁴ Telecommunications Act of 1996, Pub. L. 104-104, 110 Stat. 56 (1996).

month, the incumbent should not be allowed to claim that it needs a universal service subsidy of \$2 in order to match competitors and maintain its revenue requirements. Likewise, if an incumbent's costs are \$30 but a new entrant can provide service for \$20, universal service subsidies should not be made available to allow the incumbent to recover its inflated costs. Universal service support must not be a mechanism to guarantee incumbent providers' revenues, recover incumbents' costs, or keep them revenue neutral. The costs for maintaining such inefficient artificial support mechanisms are ultimately borne by the public.

The Telecommunications Act prohibits use of universal service support to recoup competitive losses. It prohibits cross-subsidization of competitive services with services subsidized using universal service support mechanisms.⁵ Thus, in determining the size of universal service support, the Commission and the Joint-Board should not include any assessment of competitive losses.

A common assertion in the telephone industry is that local telephone service is provided below cost, and that subsidies are required to maintain those below cost offerings. The states that have examined the evidence have found the assertion to be completely untrue -- local service is not priced below its costs.⁶ The bundle of services that incumbent local exchange carriers offer to local service customers, both residential and business customers, is profitable. If it was not profitable, competitors like WinStar would not be entering the market and

⁵ 47 U.S.C. §254(k).

⁶ For example, the Oregon Public Utility Commission Staff found that both local residential and business services to be priced above their long run incremental costs. *In the Matter of the Application of Electric Lightwave, Inc. for a Certificate of Authority to Provide Telecommunications Services in Oregon*, Order No. 96-021, at 52-58 (Or. P.U.C. January 12, 1996). In other states, Commissions regularly find that the incumbent local exchange carriers have failed to demonstrate that, taken as a whole, local services are unprofitable or that there are any carrier of last resort costs imposed on the incumbent. See, for example, *Application of MFS Intelenet of Pennsylvania, Incorporated for a certificate of public convenience and necessity*, Docket No. A-310203F0002, et al., at 23 (Pa. P.U.C. October 4, 1995); *In re: Determination of funding for universal service and carrier of last resort responsibilities*, Docket 950696-TP, at 22-23 (Fla. P.S.C. December 27, 1995); and, *Washington Utilities and Transportation Commission v. US West Communications, Inc.*, Docket Nos. UT-941464, *et seq.*, at 38 (Washington Utilities and Transportation Commission, December 27, 1995).

incumbent local providers would welcome the opportunity to shift their “unprofitable” residential customers to their competitors.

Even if local service were priced below the incumbent’s costs, in a competitive environment, below cost offerings may be entirely appropriate, and should not be subsidized by a federal universal service support program, in at least three instances: (1) where an inefficient firm has reduced its prices to compete with more efficient competitors; (2) where a firm hopes to market other more lucrative services to customers and uses the below cost offering to attract customers; or, (3) where a firm is ordered to maintain below cost rates by state commissions.

For example, it might cost a local telephone company \$45 a month to provide residential local telephone service, but a cable television company might offer cable television services for \$25 a month, upgrade its cable television network and add local telephone service for an additional \$10. The additional \$10 charge may well cover the cable television company’s incremental costs of adding telephone service even though they would not cover the telephone company’s stand-alone costs of \$45. Likewise, for wireless providers like WinStar, it may cost them far less to provide local service using their technologies than it costs the incumbent provider that uses inefficient wireline technology. In a competitive market, if it wishes to retain its customers, the incumbent will have to match or beat the prices of more efficient competitors even if that means pricing below its embedded costs. It would be inappropriate public policy to subsidize the incumbent’s efforts to price compete. Universal service subsidies should not be developed to subsidize an incumbent company’s higher stand-alone costs when new entrants using more efficient technologies or offering a different bundle of services can add telephone service for far lower incremental costs.

Broadly speaking, telephone service revenues consist of local service revenues, vertical service revenues (e.g., call waiting, call forwarding, voice mail, etc.), information services,

access revenues paid by long distance carriers, and toll service revenues. In a competitive environment, a firm may offer local service for far less than stand-alone costs in order to have the opportunity to capture the other revenue streams generated by a customer. Bell Atlantic's Chief Executive Officer, Raymond Smith applied this to telephone service when he predicted, "I can envision one day offering various packages of services. And one of them might be a package of video and interactive services in which the customer also gets phone service for another two or three bucks."⁷ Obviously, universal service support mechanisms should not subsidize such market-driven below cost offerings.

Incumbent local telephone companies often claim that state regulators force them to maintain prices below cost. If state regulators require that incumbent firms maintain local service prices far below the national average or far below costs, then it is the responsibility of the state to develop funding mechanisms to support such offerings. The Federal universal service support mechanisms that the Commission and the Joint-Board develop in this proceeding should not be sized or designed to fund state programs aimed at maintaining unusually low local service rates. In other words, it would be unmanageable if federal universal service funds were collected for state universal service programs.

Universal service support in a competitive environment, if any, should be narrowly targeted. It should be provided only in the limited instances where, in a competitive market, individuals could not afford telephone service. Since the Commission presently has successful programs aimed at subsidizing service to low income individuals (*i.e.*, Lifeline and Link Up),⁸ it is not clear that any additional universal service support mechanisms should be developed.

⁷ D. Kline, *Align and Conquer*, 3.02 WIREd 100, 164 (Feb. 1995).

⁸ Notice at ¶¶ 61-65.

II. UNIVERSAL SERVICE SUPPORT MUST BE COMPETITIVELY NEUTRAL

A. Competitive Neutrality is the Overarching Legislative Intent of the Telecommunications Act

The legislative intent of the Telecommunications Act is “to provide for a pro-competitive, de-regulatory national policy ... opening all telecommunications markets to competition.”⁹ In a competitive environment, a firm’s revenues and earnings depend entirely on its own efforts. In a competitive market, a firm’s revenues and earnings are not guaranteed by payments from competitors. The Commission and the Joint-Board should develop universal service policies that are competitively neutral and consistent with this pro-competition legislative intent.

The intent that universal service support be competitively neutral is evident throughout the universal service provisions of the Telecommunications Act. For example, Section 254(k) expressly prohibits subsidies from non-competitive services to competitive services. “A telecommunications carrier may not use the services that are not competitive to subsidize services that are subject to competition.”¹⁰ Also, Section 254(e) requires that recipients of universal service support use it only for the services for which the support is intended,¹¹ and Section 254(h)(2) requires that “the Commission shall establish competitively neutral rules” for the provision of advanced telecommunication services to schools and libraries.¹² Congress’ intent that the provision of universal service support be competitively neutral is evidenced by the principles of universal service which require that “all providers of telecommunications

⁹ Telecommunications Act, Conference Report, p. 1.

¹⁰ 47 U.S.C. §254(k).

¹¹ 47 U.S.C. §254(e). “A carrier that receives such support shall use that support only for the provision, maintenance, and upgrading of facilities and services for which the support is intended.”

¹² 47 U.S.C. §254(h)(2).

services” should contribute to universal service,¹³ and the requirements of Section 254(d) that “[e]very telecommunications provider that provides interstate telecommunications services shall contribute, on an equitable and nondiscriminatory basis, to the specific, predictable, and sufficient mechanisms established by the Commission to preserve and advance universal service.”¹⁴

If the Commission develops universal service subsidies, it is critical to maintaining competitive neutrality that such subsidies be available to any competitor that provides the subsidized service. For example, it would be inappropriate for universal service subsidies to be made available to incumbent service providers but not available to new entrants. Said differently, universal service subsidies must be completely portable to ensure competitive parity.

B. High-Costs Must be Evaluated Based on a Forward-Looking Basis, which must Consider More Efficient Technologies, like Wireless Technologies

Universal service support, if any is required in a competitive environment, can only be competitively neutral so long as it is based on the technologies and costs of competitive companies, and not the embedded technologies and costs of incumbent service providers. In its Notice, the Commission seeks comments on various proxy cost models, including the Benchmark Costing Model developed by MCI, NYNEX, Sprint and US West to estimate the loop costs of providing service to residential customers at a census block level.¹⁵ Basically, the model, like other proxy cost models, develops hypothetical loop costs using the locations of incumbent local exchange carriers’ end-offices and extending various types of wireline facilities from those end offices to census blocks. The costs are driven by the cost of fiber, copper or

¹³ 47 U.S.C. §254(b)(4).

¹⁴ 47 U.S.C. §254(d).

¹⁵ Notice at ¶¶ 31-36

coaxial cable, the density of the census blocks, and the difficulty of placing these cables in various types of terrain (e.g., water table depth, soil type, rocks, etc.). In theory, the model identifies high-cost census blocks thereby targeting universal service assistance to those areas.

The Benchmark Costing Model is a significant improvement over support mechanisms that use an incumbent's revenue requirements or costs. However, because it assumes a wireline technology the Benchmark Costing Model does not reflect the costs of competitive wireless local service providers, like WinStar. This flawed assumption creates at least three major policy implications:

- ▶ First, areas that are identified as high-cost using a wireline technology may not be high-cost if a wireless technology were employed, thereby, dramatically and artificially inflating the total subsidy borne by telecommunications firms.
- ▶ Second, if subsidies flow to companies based on a high-cost wireline assessment when a wireless technology is more efficient, those subsidies will discourage incumbents from adopting more efficient technologies and reward incumbents for maintaining inefficient facilities. This will stymie market entry by new, more efficient competitors, retard competition and will limit consumers' choices among local service providers ultimately resulting in the higher prices of a monopoly marketplace.
- ▶ Third, entry and competition by wireless competitors will be seriously distorted if subsidies flow to high-cost wireline firms. Providing universal service subsidies to high-cost wireline incumbents would be like subsidizing IBM because it has high costs and has chosen to focus on high-end, mainframe computers rather than smaller, more efficient personal computers and software. To add insult to injury, universal service principles would require personal computer manufacturers who are more efficient than IBM to provide IBM's subsidy. If a service area is identified as a high-cost service area

eligible for universal service subsidies, it is critical that the high-cost classification be true in a competitive environment based on a forward-looking analysis of costs using all feasible technologies.

C. Universal Service Support Should be Available to Any Provider that Provides Supported Services

Universal service support should not be available exclusively to the incumbent local exchange carrier, but should be available to any service provider that provides local telephone service to targeted customers or targeted high-cost service areas eligible for universal service support. Obviously, it would not be competitively neutral if universal service support were available only for incumbent service providers. New entrants will be incented to provide service to targeted customers or areas targeted for universal service support only when they have the same access to universal service support as do the incumbent competitors. Additionally, beyond the evident public safety and emergency benefits which accompany the presence of redundant systems in a service area, new entrants often possess the advanced technology necessary to deploy the required grade of telephone service greater speed and more flexibility than that offered by the incumbent.

Under the Telecommunications Act, all eligible telecommunications carriers "shall be eligible to receive support"¹⁶ and an eligible telecommunications carrier is any carrier that offers the services defined by the Commission to encompass universal service and advertises the general availability of such services. Thus, the Telecommunications Act does not reserve universal service support to incumbent carriers, but plainly intends that it be made available to any eligible carrier. If WinStar, or any other local exchange carrier, is an eligible carrier, then,

¹⁶ 47 U.S.C. §214(e)(1).

as required by the Telecommunications Act, it must receive the same universal service funding that is available to the incumbent.

D. Universal Service Support Mechanisms Must be Administered by a Neutral Third Party

In order to ensure competitive neutrality, universal service support mechanisms must be administered by an entity that has no economic or competitive interest in who receives or who provides universal service support.¹⁷ Traditional coordinating agencies, such as NECA or BellCore, are inappropriate for universal service administration because of their affiliations with incumbent local exchange carriers and the Bell Operating Companies. WinStar suggests using an independent non-governmental fund administrator to oversee universal service collection and distribution rather than state public utility commissions. Burdening state utility commissions with administration of a federal universal service fund will add to an already full agenda for many states, and some smaller states may not be staffed for the task.

III. UNIVERSAL SERVICE SUPPORT SHOULD BE EXPLICIT

The Telecommunications Act requires that any universal service support be explicit,¹⁸ “specific, predictable and sufficient”¹⁹ and collected from every interstate telecommunications carrier on an “equitable and nondiscriminatory basis.”²⁰ The conference committee report similarly indicates that Congress intended that any universal service support be explicit.

¹⁷ Notice at ¶¶ 127-131.

¹⁸ 47 U.S.C. §254(e). “Any such support should be explicit and sufficient to achieve the purposes of this section.”

¹⁹ 47 U.S.C. §254(d).

²⁰ *Id.*

To the extent possible, the conferees intend that any support mechanisms continued or created under new section 254 should be explicit, rather than implicit as many support mechanisms are today. In addition, the conferees do not view the existing proceeding under Common Carrier Docket 80-286 ... as an appropriate foundation on which to base the proceeding required by new section 254.²¹

Universal service support should be explicit in that it should consist of payments that are used only for the provision of services comprising universal service. In its Notice, the Commission observed that universal service support is provided through a variety of implicit and explicit mechanisms, including the Universal Service Fund ("USF") and Dial Equipment Minute ("DEM") weighting which provide support to smaller local exchange carriers in high-cost service areas,²² Lifeline and Link Up programs for low income subscribers,²³ recovery of the interstate allocation of loop costs through a combination of subscriber line charges ("SLCs") paid by end-users and carrier common line charges ("CCLCs") paid by long distance carriers,²⁴ and long term support ("LTS") paid by larger local exchange carriers.²⁵ Universal service subsidies, if required at all in a competitive environment, must be made explicit and replace the complex, arcane maze of subsidies that today are allegedly used for universal service support.

IV. CONCLUSIONS

WinStar, a provider through its operating affiliates of competitive local telecommunications services, recommends that as the Commission and Joint-Board develop universal service mechanisms they focus on the impact that such policies and mechanisms

²¹ Joint Explanatory Statement of the Committee of Conference, p. 131.

²² Notice at ¶¶ 14, 40-45.

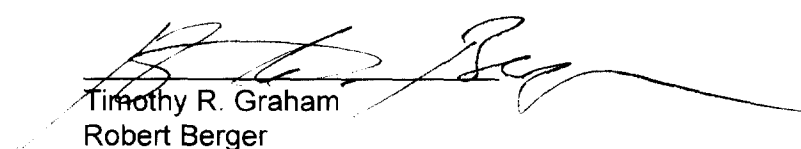
²³ Notice at ¶¶ 61-65.

²⁴ Notice at ¶¶ 112-114.

²⁵ Notice at ¶ 115.

have on the development of competition. Because competition creates incentives for firms to reduce prices and costs, WinStar believes that the Commission and Joint-Board can presume that competition will advance universal service, and universal service support should be provided only in extraordinary circumstances. As described in these comments, WinStar demonstrates why universal service support must be competitively neutral and cannot be used as a mechanism to maintain the incumbent provider's revenues or recoup investment in its embedded plant. Winstar recommends that universal service support, if any, should be available to any eligible carrier and based on the forwarding looking costs of the most efficient service provider, which may be a wireless provider like WinStar and not the wireline incumbent.

Respectfully submitted,



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Dated: April 12, 1996

CERTIFICATE OF SERVICE

I hereby certify that on this 12th day of April 1996, copies of the foregoing
COMMENTS OF WINSTAR COMMUNICATIONS, INC. in Docket 96-95, were served
via Messenger** or First-Class Mail, U.S. postage prepaid, to the parties on the
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